Prince Edward Island
CANADA

PEI LENDING AGENCY

Annual Report 2003-2004

105-03775/

Message from the Minister Designate

The Honourable J. Léonce Bernard
Lieutenant Governor of Prince Edward Island
PO Box 2000
Charlottetown, PE C1A 7N8

May It Please Your Honour:

Pursuant to the *PEI Lending Agency Act* and
as minister designate for the time period
covered by this report,
it is my privilege to submit the Annual Report
of the PEI Lending Agency
for the period ending March 31, 2004.

Respectfully submitted,

Mitch Murphy
Provincial Treasurer

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Message from the Board Chair

June 30, 2004

The Honourable Mitch Murphy
Provincial Treasurer
Province of Prince Edward Island

Dear Minister:

On behalf of the board of directors of the PEI Lending Agency, I take pleasure in once again presenting you with this, the Annual Report of the agency for the fiscal year ending March 31, 2004.

This report is being presented pursuant to the *PEI Lending Agency Act* and Regulations.

Sincerely,

W.R. Noonan
Chairman, Board of Directors
PEI Lending Agency

Message from the Chief Executive Officer

Mr. William Noonan, Chairman
Board of Directors
PEI Lending Agency

Dear Mr. Noonan:

I am pleased to present the Annual Report of the PEI Lending Agency for the fiscal year 2003-2004.

As evidenced in the financial statements of the agency, if it were not for a further advance from the province, the agency would have experienced a loss for the second consecutive year. The increased need for additional funds in excess of those budgeted were the result of a need for an increase to the provision for future loan losses, as recommended by the agency's auditors.

There have been many problems impacting Island industry over the past year, such as, low hog prices, decreased tourism visitation, closed borders for beef, low lobster landings for PEI south-side fishermen and various problems within the oyster fishery. These factors have had a marked influence on agency clients and, consequently, operations. The Information Technology boom has slowed, as has the rapid growth experienced by the aerospace industry prior to September 2001. When combined, little opportunity remains for positive portfolio growth.

On a more favourable note, primary industries are generally cyclical with high and low periods being recognized as the norm. As the province's principal lender, the agency maintains a level of flexibility which it exercises when and where-ever possible, to help sustain businesses through these difficult periods. Cooperative assistance with line departments has increased to include relief programs for the beef industry and expanded support to the hog industry. We will continue to participate in similar initiatives when reasonable solutions can be identified which have the potential to maintain key industries through similar downturns.

To achieve the agency's objective of being a break-even operation may require a five-year cycle, due to regular industry highs and lows. Management has begun a preliminary review of operations with a view to the feasibility of an expanded mandate aimed at growing a more balanced portfolio. The concept being that inclusion of more solid, profitable business clients would help offset the riskier or more developmental ventures. This change would help improve the financial bottom line of the corporation and ultimately eliminate or significantly reduce the level of possible losses to the province.

Management and staff continue to strive to support the objective of sustaining and growing local industry while exercising responsible lending practises aimed at minimizing the financial risk to the province.

Respectfully submitted,

P.A. Wilson
Chief Executive Officer

Mandate of the PEI Lending Agency

The mandate of the PEI Lending Agency is to provide financial assistance, through loan agreements, in support of the Government's economic development strategy and to support enterprises that demonstrate reasonable viability, though are unable to access private sector financing or the terms and conditions required to meet their needs.

The agency is to operate as a responsible, professional lender, basing decisions or recommendations on sound lending practices. Under the authority of the *PEI Lending Agency Act* and Regulations, the board of directors, consisting of six private sector and two Government-designated directors, provide agency staff with consistent guidance and direction. They strive to meet the needs of Island industries and individual businesses throughout the constantly shifting priorities and challenges which may evolve as a result of local provincial issues or from various constraints imposed by national and international markets.

Though the general mandate of the agency will remain unchanged, the focus may be altered in favour of specific industries, at Government's direction, or through identifiable gaps which may emerge in commercial bank financing. With their singular objective of profitability and with policy decisions which are generally nationally directed, there will always be areas or gaps left by the banks that the agency will be needed to fill.

As the province's primary lending arm, the agency will undoubtedly continue to collaborate with other Government departments and corporations to structure financial programs to promote new development or to assist industry-specific difficulties. It continues to support the needs of our primary industries for capital purchases, expansion and operational expenses as well as encourages financing of non-traditional, potentially prosperous new enterprises.

The agency is unquestionably a higher-risk lender and often lender of last resort. Where any business can continue to demonstrate a potential for viability, the agency is generally supportive of providing assistance as it will maintain current employment while offering the operator the opportunity for recovery. This is a role the agency has historically provided and numerous businesses have been ultimately successful due to this support in difficult times. Also, differing from the commercial banks' profit requirement, the agency's mandate is to strive for a break-even operation. If this can be achieved, there are numerous benefits to the province, in various capacities, but no cost to the taxpayer for the service. By sustaining businesses and maintaining employment, it reduces the drain on already stressed provincial and federal support programs. In addition, revenue from business, personal and sales taxes is maintained. These are all valuable considerations and are weighed, along with various other factors, when decisions are made by agency staff.

Corporate Profile

The PEI Lending Agency was established to provide both term and working capital loans to eligible borrowers in the following sectors:

Small Business

Definition – Small business includes any person who:

(i) *carries on business, or intends to carry on business, in the province;*

(ii) *purchases a finished product from a supplier and resells that product without alteration;* and

(iii) does not employ more than 100 employees; or

(iv) did not have annual gross sales exceeding $10 million in the fiscal year immediately preceding an application made pursuant to Section 9 of the act.

This program is designed to meet the special needs of the Island's small business community and entrepreneurs for business acquisitions, expansions and debt consolidation.

Agriculture

Definition – Agriculture includes any person who:

(i) *carries on business, or intends to carry on business, in the province;*

(ii) owns or will acquire farm assets with the loan proceeds pursuant to the act or the regulations; and

(iii) is actively engaged in farming or intends to work actively at producing farm products.

It is the objective of the agency to encourage increased production of both established and new variety agricultural products, as well as, improved marketing facets and techniques for PEI agricultural products. This may include better storage, handling, grading and packaging facilities.

Tourism

Definition – Tourism includes any person who:

(i) *carries on business, or intends to carry on business, in the province; and*

(ii) operates a business, other than a Bed & Breakfast establishment as defined in the Tourism Industry Act Regulations (EC267/99), that holds a valid tourism establishment licence issued pursuant to the Tourism Industry Act Regulations.

Projects to expand the shoulder tourist season and development of integrated recreational complexes which would feature entertainment facilities, lodging and dining facilities are encouraged. In some cases, loans may be granted for accommodation units which are converted to other uses during off-season periods.

This program is designed to meet the special needs of Island tourism operators for business acquisitions, expansions and debt consolidation, refurbishment of fixed assets and in some cases working capital for seasonal startup.

Bed & Breakfast operations, as defined by the *Tourism Industry Act* Regulations, are ineligible to borrow from the agency.

Manufacturing and Processing

Definition – Manufacturing and processing includes any person who:

(i) *carries on business, or intends to carry on business, in the province; and*

(iii) operates a business which produces a product by mechanical method from a raw material that is altered to add value.

Loans are available to finance land and buildings, specialized equipment, and in some cases, production inventory.

Fisheries and Aquaculture

Definition – Fisheries and Aquaculture includes any person who:

(i) *carries on business, or intends to carry on business, in the province; and*

(ii) is licensed or qualified to obtain a licence or aquaculture permit issued by the federal Department of Fisheries and Oceans, for any of the commercial fisheries or aquaculture industries in the province.

The objective of the agency is to provide term financing, recapitalization and operating lines of credit to assist applicants in the commercial fishery and/or aquaculture industry. The agency takes a particular interest in supporting projects that have a potential commercial viability for under-exploited species of finfish, shellfish and sea plants.

Information Technology

Definition – Information technology includes any person who:

(i) *carries on business, or intends to carry on business, in the province; and*

(ii) operates a business that derives at least 60 per cent of revenue from software publishing, computer systems design and related services, the provision of online information services, or the manufacture of computer and peripheral equipment or related electronic components.

The objective of the agency is to provide term financing and operating lines of credit to assist borrowers purchasing fixed assets and for production and marketing expenses.

Aerospace

Definition – Aerospace includes any person who:

(i) carries on business, or intends to carry on business, in the province;

(ii) owns or will acquire assets of an aviation or aerospace-related business with loan proceeds received pursuant of the act or the regulations; and

(iii) is actively engaged in or intends to work actively in an aviation or aerospace-related business.

Year in Review

Over the past year, the agency saw an increase in loan applications from 128 in 2002/2003 to 172 in 2003/2004. This significant increase is due, however, primarily to receipt of 52 applications for financing under the Beef Loan Program. While the agency recorded a significant increase in applications within the small business and tourism sectors, the remaining sectors experienced a decrease. Additionally, the portfolio also saw a reduction to the number of loans and the number of clients, as well as a drop of $3.4 million to the outstanding balance of the entire portfolio on a year-over-year comparison.

As noted throughout this report, the primary industries of PEI have all experienced more than their share of difficulties this past year. Potato growers have seen only one good year out of the past four, that being 2002, when both prices and yields were good. The surplus production of 2003, which led to depressed markets and low prices, further compounded financial difficulties which were experienced as a result of the problems of the 2000 and 2001 years – ones from which producers hadn't yet fully recovered. The agency's portfolio of blueberry clients has remained relatively stable since the implementation and receipt of interest relief subsidies from the Department of Agriculture, Fisheries and Aquaculture.

Problems were also experienced within both the fisheries and tourism industries which were, in large part, difficult to avoid for those who invested in these particular sectors. Following the opening of the Confederation Bridge and the subsequent increase of tourists, operators geared up to ensure they could accommodate much larger numbers in future. Unfortunately, there's been a gradual decrease in tourist numbers since that time. Whether the novelty of the bridge itself is slowly fading or whether it may be due to other factors is difficult to assess. Events such as the war in Iraq, high fuel costs, BSE and SARS may have all played a part in the decreased visitation.

As long as participation in the public fishery is at maximum sustainability, there can be no growth to this industry. If the low landings recorded the last couple of years is any indicator, this may be the current case within the lobster fishery. It is more likely the industry will see a decrease to numbers in future, rather than the reverse. Similarly, it is difficult for the agency to grow this particular portfolio of clients. New applicants are often those experiencing financial difficulties; and, in those such instances, agency staff will attempt to assist wherever it can be determined that there remains a reasonable possibility for recovery. It is expected any future growth to this sector will likely be through cultured products.

Overall, the agency's entire portfolio decreased year-over-year by $3.4 million. This was distributed among various sectors of the economy excluding the agriculture, fisheries and tourism portfolios, which experienced slight growth. The number of loans decreased slightly from March 31, 2003, with only the agriculture portfolio showing an increase and, as noted, that was due to the added Beef Program clients. There has been a slight year-over-year decrease in loan arrears at March 31, 2004, with $9,733,129 owing in payments and $13,774,249 being the outstanding balance of those accounts. Both these figures include entire loan balances of any loan which has been placed in non-current status.

For the period ending March 31, 2004, there was a need for the agency to increase its budgeted loan loss provision amount by $2.4 million. This increase was warranted as there were two significant accounts and a number of smaller loans, in which early indications suggest a loss may be eminent. As profitability from operations was insufficient to fund this increase, the agency was required to source the funds from the province. At the same time, management also sought a further $1.3 million to offset the deficit remaining from fiscal 2002/2003. For the benefit of the reader, a provision for loan loss is simply an amount set aside, typically from profits, to be used in a year when there may be insufficient funds to cover all loan losses. As

for the actual losses experienced by the agency during fiscal 2004, this amounted to $957,750.

Despite the setbacks experienced by our particular industries, at both the provincial and national level, management is optimistic that, in a number of cases, these setbacks are representative of temporary issues or caused by unique circumstances unlikely to be permanent or long lasting. Agency management will continue to explore various options with industry and Government interests in order to maintain the provision of valuable financial support to our industries while at minimal cost to the province.

Small Business

The Lending Agency received a total of 20 loan applications, totalling $3.3 million in requested financing, for the small-business sector during the year ending March 31, 2004. From this figure, 16 loans were approved for a total of $2.9 million while four applications were declined. Approximately 60 per cent of the loans approved were for the purchase of capital assets and the remaining 40 per cent being for debt consolidation.

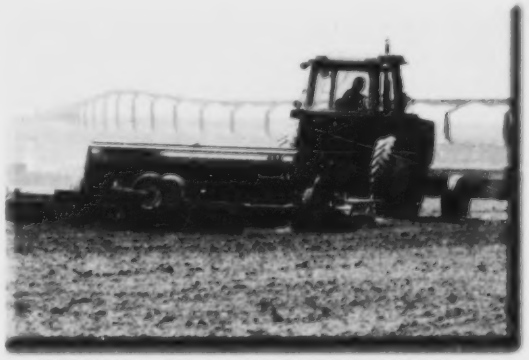
Though the number of clients and size of the portfolio has decreased, year-over-year, the number of applications received this year is a 67 per cent increase over the previous year. In fiscal 2001/2002 the agency saw a sharp decrease in applications for small business enterprises and that decrease continued into 2002/2003. Hopefully, the current increase is a trend that will see more prosperity within this area of Island business. At this point, we anticipate there may be a small increase to applications for the coming year.

Agriculture

The agency continues to play a significant role in providing financing to the agricultural sector. Agricultural loans comprise approximately 25 per cent of the total lending portfolio, however, they account for approximately 50 per cent of the agency's clients. Working capital loans to clients in the potato industry represent some of the larger individual projects. The total agricultural portfolio as of March 31, 2004, increased by $2 million from $34.1 million to $36.1 million from the previous year. This increase was due entirely to loans provided for working capital purposes. Of the 92 applications approved, 86 were for working capital.

The 2003 season was an excellent growing year, however, potato farmers are experiencing one of the poorest years on record due to depressed markets. It's estimated there is approximately 20 per cent surplus production which will result in many producers having working-capital shortfalls. Those with equity in their operations may be approaching financial institutions for debt consolidation. It's also anticipated the agency will receive requests to provide funding to potato operations which traditionally have been financed by the banks/credit unions. Unfortunately there will be casualties since not all can be accommodated.

The hog industry is also having a difficult year as market prices were significantly below breakeven for most of the year. As in other provinces, the trend is toward larger operations which require substantially increased financing.



It is highly unusual to have the three main sectors within the agricultural industry experiencing difficulties at the same time but this was the case over the past year. In addition to the problems which have plagued potato and hog farmers, beef farmers have also been negatively affected by poor market prices since the initial discovery of BSE or "mad cow" in May 2003. As most people are aware, this discovery resulted in the USA closing its border to Canadian beef. A further discovery of another BSE case in the USA, which was traced back to an Alberta ranch, further hampered the Government's efforts to have the border opened.

This resulted in the agency providing a cash flow loan program for beef producers, similar to that provided to hog producers in the past, to help ease the producers' current strain on cash flow. On a positive note, it's anticipated that the new beef processing plant, with a planned opening on PEI in the fall of 2004, will improve the local market. All factors point to the

requirement for continued financial support to this area of Island business in the coming year.

It is noteworthy that producers of supply-managed commodities such as dairy, eggs and poultry do not appear to be experiencing the financial difficulties of those engaged in non-supply-managed commodities.

The blueberry industry on PEI has now become a significant industry. In 2003, producers harvested 7.4 million pounds of fruit which is the largest harvest ever recorded. Overall, it was a good growing season and crop yields continue to increase as more developed land comes into production. Cranberries on the other hand remains a much smaller industry, however, production is increasing annually now that a number of cranberry bogs are producing their second crop. The total crop harvested in 2003 was estimated at 300,000 pounds.

As in the past several years, the agency continues to administer a number of programs for the Department of Agriculture, Fisheries and Aquaculture. This includes the Ranched Fur Advance Payment Program, Hog Cash Flow Bridge Loan Program, and the Hog Depop-Repop Program.

The agency is well positioned, because of its experienced agricultural lenders, to continue supporting traditional producers, as well as evaluating new ventures. This could include playing a major role in financing the development of any new alternative crops. It also continues to work closely with other financial institutions in an effort to share the financial risk.

Tourism

The Lending Agency received 19 loan applications for a total of $9.3 million by the tourism sector for the fiscal year ending March 31, 2004. From this figure, 17 loans were approved, for a total of $3.4 million, one application was declined and one for $5.8 million was still pending at year-end. This is a significant increase from the year prior which saw only nine applications received. Of those nine, eight were approved for a total of $2.6 million in financing. The total loans outstanding, at March 31, 2004, was $16,147,000 which represents an increase of 6.6 per cent over the previous year in the loan balance.

Visitation to PEI decreased 3.8 per cent from 1.149 million visitors in 2002 to 1.105 million in 2003. Tourism spending also decreased 2.1 per cent from $352.9 million in 2002 to $345.6 million in 2003. This translates into a minor increase to arrears in the agency's tourism accounts. At March 31, 2004, five clients were in arrears with $151,000 in past due loan payments, which is 0.9 per cent of the tourism portfolio.

The majority of funds advanced were requested for the purpose of purchasing existing operations and for renovations to older establishments. As statistics indicate there is sufficient fixed-roof accommodations to service the industry, it is expected the majority of future financing requests will be for similar purposes.

Management anticipates a modest increase to the dollar value of applications in the coming year.

Manufacturing and Processing

The agency's portfolio of M&P clients continues to remain highly diverse, generating most income from export trade. Our clients are involved in a wide cross-section of industries including biochemical production, snack food processing, industrial and retail metal fabrication, production of sea vessels, food processors, mass-transit component manufacturing, and resource-based value-added production companies, to name a few. Overall, this portfolio remained virtually unchanged (0.4 per cent decline), despite receiving 18 applications. While we remain open to applications from new clients, growth continues to be generated primarily from our existing client base.

The agency received a total of 18 applications this year in the amount of $13,007,600 in comparison with 19 applications received last year. Of the applications received, 15 received approval and three were declined.

Excluding two larger applications, the average application request amounted to $156,725. At year-end our loan exposure to the manufacturing and processing industry totalled $55,409,557 representing 35.6 per cent of the agency's total portfolio.

Despite being a strategic lender, we perform the same due diligence practices as do the traditional financiers in measuring the risk associated with any application. In some cases the risks are greater, however, the strategic aspects of applications warrant investment that may not otherwise be available to the borrower, to generate new economic activity unique to the Island. During the period under review, we have experienced one particularly large loan influencing the material loss reported. While regrettable, this is a cost of doing business as a crown corporation and for this reason, we establish loan loss provisions. No additional write-offs are anticipated for which a provision for bad debt has not already been established.

From a risk standpoint, the overall health of our manufacturing and processing portfolio remains strong. Though the volatility of foreign currency fluctuations has, in some cases, adversely impacted the profitability of some of our clients, it is not to the extent that our investments are in jeopardy.

We remain focussed on maintaining a balance between providing sound loans to established Island companies and to supporting new enterprises, where the risks are deemed acceptable.

Fisheries and Aquaculture

In fiscal year 2003/2004, 22 applications were received for a total of $2 million in requested financing. Of those applications, 21 were approved for a total of $1.9 million. The one remaining application was withdrawn. This represents an increase of three applications received and an increase of $300,000 requested financing over the previous year.

Of the applications approved, six represent working capital loans to mussel farming operations and one was for the lobster fishery. The remaining 14 loans were for term financing for the purchase of vessels, equipment, fishing enterprises and/or debt consolidation. Eleven of these loans were provided to traditional fisheries clients and four were to mussel farmers.

The fisheries and aquaculture portfolio of clients decreased from 108 to 104 over the previous year. However, our total investment into this sector increased from $10.7 million to $11.7 million. The problems encountered in the oyster farming industry have resulted in an additional seven clients, representing aggregate loans totalling $2.5 million, being placed into a non-current status. These clients are in various stages of wind-up and/or filing for bankruptcy. The ultimate losses to the agency are expected to be high, exceeding the $2 million figure. There are only five remaining oyster farm clients whose loans are in a current status, of which only four are expected to maintain continued viability and meet their obligations.

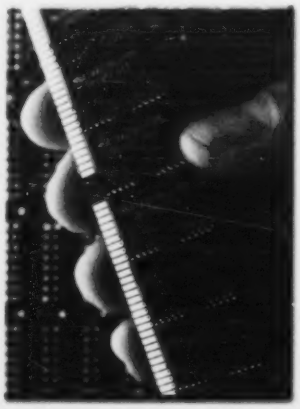
The traditional lobster fishery has seen the north side of the province experiencing increased landings with clients meeting agency repayment terms. Conversely, both the spring and fall lobster fisheries in the Northumberland Strait have experienced reduced landings, resulting in the agency re-negotiating repayment terms on a case-by-case basis. More specifically, the Northumberland Strait fishery reduction has resulted in eight clients' loans being re-written to capitalize arrears and attempt to decrease repayment requirements to match the reduced income levels. If the decline in lobster landings in the Northumberland Strait continues, this will have a major impact on the agency's fishery portfolio, as 40 of our clients (out of a total of 92) fish this area.

Hopefully, in future, the increased lobster carapace size will allow for a return to higher lobster landings in the Northumberland Strait, enabling future repayment of Lending Agency accounts. In the interim, the agency will need to continue to restructure existing loan agreements, as needed, where there is demonstration of an ability to repay obligations over time. Without such, many fishermen would be forced to exit the industry, inevitably resulting in a loss to the agency.

The agency continues to manage and monitor this portfolio closely, at present, to mitigate the risk of future potential losses.

Information Technology

Asset-based lenders are typically challenged by finding ways to extend financing to companies operating within this industry, given the typical structure of a balance sheet comprised predominantly of intangible assets such as software, deferred development costs, copyrights, patents, etc. Combined with the volatility associated with the industry itself, financing is often provided by vendor, venture capital, angel or owner equity, in lieu of debt.



Following the revision of the Lending Agency Regulations establishing information technology as its own distinct sector, the challenge for the agency has been to find a palatable solution, agreeable to all funding partners, that envisioned a combination of debt and equity to see IT projects materialize. This is not always an easy task.

Since March 2001 when the agency's exposure to IT companies totalled $3.3 million, there has been a steady decrease in the portfolio to its current level of $1.5 million, making it the agency's smallest sector portfolio, accounting for only one per cent of the total outstanding loans.

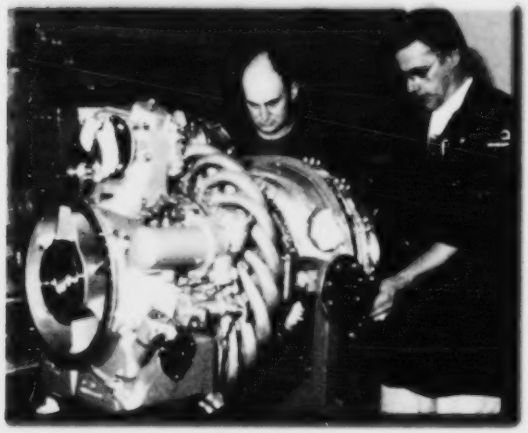
Aerospace

Companies classified in this sector are involved either in the construction of, or providing parts for, aircraft. Currently, the agency provides financing to businesses involved in the repair and overhaul of fixed-wing aircraft, original equipment manufacturing and commercial passenger service. For the period ending March 31, 2004, the agency did not receive any applications or experience any growth in the portfolio which may be attributed to a number of reasons.

First, there has been tremendous growth in Slemon Park, in terms of physical expansion over the last three to four years, with the establishment of MDS-PRAD Technologies Corporation and the further expansions of Testori Americas International and Atlantic Turbines Inc. We expect that further expansion will be minimal and, instead, these past efforts will be translated into sales.

Secondly, the larger multinational companies are, for the most part, self-financing. Those companies within Slemon Park that are either publicly traded or contain the borrowing capacity to access cash directly from money markets are able to finance expansion and working capital requirements far more cheaply than can be provided by either a traditional or this Government lender.

Overall, the associated business risk is not well disbursed among a large number of clients, but despite the volatility and uncertainty of operating within this industry, the agency's clients continue to perform well. The loan exposure at year's end totalled $19,980,000, representing 12.8 per cent of the total loan portfolio.



Compte rendu de l'année

Au cours de l'année écoulée, l'Agence de crédit a constaté une augmentation des demandes de prêt, qui sont passées de 128 en 2002-2003 à 172 en 2003-2004. Cependant, cette forte augmentation est due principalement à la réception des 52 demandes de financement au titre du *Beef Loan Program* (programme de prêt pour le boeuf). L'Agence a noté une augmentation importante du nombre de demandes dans les secteurs de la petite entreprise et du tourisme, mais a constaté une diminution dans les autres secteurs. En outre, le portefeuille a également vu une diminution du nombre de prêts et de clients ainsi qu'une baisse de 3,4 millions de dollars du solde impayé pour l'ensemble du portefeuille par rapport à l'année précédente.

Comme nous le signalons tout au long du présent compte rendu, les industries du secteur primaire de l'Î.-P.-É. ont toutes eu plus que leur part de difficultés au cours de l'année qui vient de s'écouler. Les producteurs de pommes de terre n'ont eu qu'une bonne année sur les quatre dernières, soit l'année 2002, alors que les prix et les rendements furent bons. La production excédentaire de 2003, qui a donné lieu à des marchés languissants et à des bas prix, a aggravé les difficultés financières occasionnées par les problèmes survenus en 2000 et en 2001 problèmes dont les producteurs ne s'étaient pas encore entièrement remis. Le portefeuille des clients de l'agence oeuvrant dans le secteur du bleuet est demeuré relativement stable depuis l'établissement et la rentrée des aides au paiement d'intérêt du ministère de l'Agriculture.

Les industries des pêches et du tourisme se sont également heurtées à des problèmes qui étaient, pour la plupart, difficiles à éviter pour les investisseurs dans ces industries. À la suite de l'inauguration du pont de la Confédération et de l'augmentation du nombre de touristes qui a suivi, les exploitants d'entreprises touristiques se sont préparés en vue d'accueillir beaucoup plus de visiteurs à l'avenir. Malheureusement, le nombre de touristes diminue progressivement depuis. Il est difficile d'évaluer si cette diminution est attribuable au fait que l'attrait de la nouveauté du pont s'estompe lentement ou si elle est attribuable à d'autres facteurs. Des événements comme la guerre en Iraq, les coûts élevés du carburant, l'encéphalopathie bovine spongiforme (EBS) et le syndrome respiratoire aigu sévère (SRAS) peuvent tous avoir contribué en partie à la diminution du nombre de visiteurs.

Aussi longtemps que la participation dans les pêches publiques sera au niveau maximal soutenu, il ne pourra y avoir de croissance dans cette industrie. C'est peut-être ce qui se passe actuellement en ce qui concerne la pêche du homard si on se fie aux faibles quantités débarquées qui ont été enregistrées, les dernières années. Il y a plus de chances que l'industrie constate une baisse des chiffres à l'avenir que l'inverse. De même, l'agence peut difficilement agrandir ce portefeuille particulier de clients. Souvent, les nouveaux demandeurs ont des difficultés financières et, dans de tels cas, le personnel de l'agence tâche de donner de l'aide chaque fois qu'il peut être déterminé qu'il reste une possibilité raisonnable de redressement. Nous croyons que toute croissance future qui pourrait se produire dans ce secteur serait attribuable aux produits de culture.

Dans l'ensemble, le portefeuille tout entier de l'agence a diminué de 3,4 millions de dollars par rapport à l'année précédente. Cette diminution était répartie entre différents secteurs de l'économie, mis à part les portefeuilles de l'agriculture, des pêches et du tourisme qui ont connu une légère croissance. Le nombre de prêts a diminué légèrement par rapport au 31 mars 2003, avec seulement le portefeuille de l'agriculture qui montrait une augmentation laquelle, comme nous l'avons fait remarquer, était due à l'ajout de nouveaux clients du programme pour le boeuf. Au 31 mars 2004, il y a eu une légère baisse sur douze mois des arriérés de prêts, avec 9 733 129 $ en paiements exigibles et 13 774 249 $ constituant le solde impayé de ces comptes. Sont inclus dans ces deux montants le total des soldes des prêts pour tous les prêts qui sont classés dans les prêts en souffrance.

L'agence a dû augmenter les provisions pour pertes sur prêts de 2,4 millions de dollars, pour la période ayant

pris fin le 31 mars 2004. Cette augmentation était justifiée parce que, très tôt, tout portait à croire que des pertes étaient imminentes relativement à deux comptes importants et à un certain nombre de petits prêts. Comme les activités n'étaient pas assez rentables pour financer une telle augmentation, l'agence a été contrainte de se procurer les fonds voulus auprès de la province. En même temps, la direction a demandé 1,3 million de plus pour équilibrer le déficit qui restait de l'année financière 2002-2003. Nous précisons à l'intention du lecteur qu'une provision pour pertes sur prêts est simplement un montant réservé, généralement sur les profits, pour être utilisé une année où il n'y aurait peut-être pas assez de fonds pour combler toutes les pertes sur prêts. Les pertes réelles subies par l'agence durant l'année financière 2004 s'élevaient à 957 750 $.

Malgré les revers essuyés par nos industries, à l'échelle provinciale et nationale, la direction est à peu près convaincue que, dans un certain nombre de cas, ces revers expriment des problèmes temporaires ou ont été occasionnés par des circonstances uniques qui ont peu de chances de perdurer. De concert avec l'industrie et le gouvernement, la direction de l'agence continuera d'examiner différentes options afin de maintenir la prestation d'une aide financière précieuse à nos industries, mais qui coûte le moins cher possible à la province.

Petite entreprise

Au cours de l'année qui a pris fin le 31 mars 2004, l'Agence de crédit a reçu au total, pour le secteur de la petite entreprise, 20 demandes de prêts qui représentaient 3,3 millions de dollars. Quatre demandes ont été rejetées. Le total des 16 demandes qui furent acceptées s'élevaient à 2,9 millions de dollars. Environ 60 % des prêts consentis l'ont été pour l'achat d'immobilisations et le reste des prêts, soit 40 %, pour la consolidation de dette.

Bien que le nombre de clients et la taille du portefeuille aient diminué, le nombre de demandes reçues cette année constitue une augmentation de 67 % par rapport à l'année précédente. Au cours de l'année financière 2001-2002, l'agence a vu une baisse brutale du nombre de demandes pour les petites entreprises, et cette baisse s'est poursuivie en 2002-2003. Il est à espérer que l'augmentation en cours constitue une tendance qui annonce une plus grande prospérité pour ce secteur des affaires de l'Île. À l'heure actuelle, nous nous attendons à ce qu'il y ait une légère augmentation des demandes pour l'année prochaine.

Agriculture

L'agence continue de faire beaucoup pour le financement du secteur agricole. Les prêts agricoles constituent environ 25 % de l'ensemble du portefeuille de prêts, mais ces prêts sont détenus par environ 50 % des clients de l'agence. Les prêts de fonds de roulement accordés aux clients de l'industrie de la pomme de terre représentent certains des projets individuels les plus importants. Au 31 mars 2004, le total du portefeuille agricole a augmenté de 2 millions de dollars, ayant passé de 34,1 à 36,1 millions par rapport à l'année précédente. Cette augmentation était entièrement due aux prêts de fonds de roulement consentis. Des 92 demandes de prêt approuvées, 86 l'ont été pour le fonds de roulement.

La saison 2003 a été une année de croissance excellente. Néanmoins, les cultivateurs de pommes de terre connaissaient l'une des pires années enregistrées à cause des marchés languissants. On estime à environ 20 % la production excédentaire, ce qui entraînera pour beaucoup de producteurs une insuffisance de fonds de roulement. Il se peut que les producteurs qui ont investi des capitaux propres dans leur entreprise sollicitent des établissements financiers pour consolider leur dette. Nous nous attendons également à ce que l'agence reçoive des demandes de financement de producteurs de pommes de terre qui étaient auparavant financés par des banques ou des caisses populaires. Malheureusement, il y aura des pertes puisqu'il est impossible d'aider tout le monde.

L'industrie du porc connait aussi une année difficile étant donnée que les prix du marché ont été de beaucoup inférieurs au seuil de rentabilité pendant une bonne partie de l'année. Comme dans d'autres provinces, la tendance est aux entreprises de grande taille qui, pour leur part, nécessitent une plus grande aide financière.

Il est très rare que trois grands secteurs de l'industrie agricole connaissent des difficultés en même temps,

mais c'est bien ce qui s'est produit pendant l'année écoulée. Outre les problèmes qui ont durement touché les cultivateurs de pommes de terre et les éleveurs de porcs, les éleveurs de boeufs ont aussi été éprouvés par les bas prix du marché depuis la découverte de l'EBS, ou « maladie de la vache folle », en mai 2003. La plupart des gens savent qu'à la suite de cette découverte, les États-Unis ont fermé leur frontière au boeuf en provenance du Canada. La découverte d'un autre cas d'EBS aux États-Unis, dont la source a été retracée jusqu'à une ferme de l'Alberta, a nui aux efforts déployés par le gouvernement en vue de faire rouvrir la frontière.

Cette situation a amené l'agence à mettre sur pied, à l'intention des producteurs de boeufs, un programme de prêts sur capacité d'autofinancement semblable à celui qui était destiné aux producteurs de porcs par le passé, afin d'aider les producteurs à tenir le coup en regard des pressions exercées actuellement sur les fonds de roulement. Sur une note positive, on s'attend à ce que la nouvelle usine de transformation du boeuf, dont l'ouverture est prévue à l'Île à l'automne 2004, permette d'améliorer le marché local. Tous les facteurs nous amènent à la conclusion qu'il faudra continuer d'aider financièrement ce secteur des affaires de l'Île au cours de l'année à venir.

Il convient de noter que les producteurs de produits soumis à la gestion de l'offre, comme les produits laitiers, les oeufs et la volaille, ne semblent pas avoir les difficultés financières qu'éprouvent les producteurs de produits non soumis à la gestion de l'offre.

L'industrie du bleuet à l'Î.-P.-É. est maintenant une industrie importante. En 2003, les producteurs ont récolté 7,4 millions de livres de fruits, soit la plus grosse récolte jamais rapportée. Dans l'ensemble, la saison de croissance fut bonne et le rendement des cultures continue d'augmenter à mesure que d'autres terres mises en valeur deviennent productives. En revanche, l'industrie de la canneberge demeure moins importante, même si la production augmente annuellement, maintenant que des marais à canneberges produisent leur deuxième récolte. On a évalué le total des récoltes à 300 000 livres, en 2003.

Comme elle le fait depuis plusieurs années, l'agence continue d'administrer un certain nombre de programmes pour le compte du ministère de l'Agriculture et des Forêts, entre autres, le *Ranched Fur Advance Payment Program* (programme de paiement anticipé pour les fourrures d'élevage), le *Hog Cash Flow Bridge Loan Program* (programme de prêt-relais pour venir en aide aux éleveurs de porc) et le *Hog Depop-Repop Program* (programme de dépeuplement-repeuplement du porc).

Grâce à ses prêteurs agricoles rompus aux affaires, l'agence est bien placée pour continuer à appuyer les producteurs traditionnels ainsi que pour évaluer les nouvelles entreprises. Elle pourrait, entre autres, avoir un rôle important dans le financement du développement de toute nouvelle culture de remplacement. Elle continue également de travailler étroitement avec d'autres établissements financiers pour essayer de partager le risque financier.

Tourisme

L'Agence de crédit a reçu 19 demandes de prêts, soit 9,3 millions en tout, en provenance du secteur touristique, pour l'année financière qui a pris fin le 31 mars 2004. Une demande a été rejetée. Les 17 demandes approuvées s'élevaient à 3,4 millions de dollars en tout et une demande de 5,8 millions n'avait pas encore été traitée en fin d'année. Il s'agit d'une augmentation importante par rapport aux 9 demandes reçues l'année précédente. Huit de ces neuf demandes ont été approuvées pour un montant total de 2,6 millions de dollars. Le total des prêts en cours, au 31 mars 2004, était de 16 147 000 $, représentant également une augmentation de 6,6 % dans le solde des prêts, par rapport à l'année précédente.

Le nombre total des visiteurs à l'Î.-P.-É. a diminué de 3,8 %, ayant passé de 1,149 millions de visiteurs en 2002 à 1,105 millions en 2003. Les dépenses engagées

pour le tourisme a également diminué de 2,1 %, ayant passé de 352,9 millions de dollars en 2002 à 345,6 millions en 2003. Cela s'est traduit par une légère augmentation des arriérés dans les comptes du tourisme de l'agence. Au 31 mars 2004, cinq clients avaient accumulés des arriérés, ce qui représentait 151 000 $ en arriérés sur les paiements de prêts, soit 0,9 % du portefeuille du tourisme.

La grande partie des fonds prêtés était destinée à l'acquisition d'entreprises existantes et à la rénovation d'anciens établissements. Étant donné que, selon les statistiques, il y a de l'hébergement en dur en quantité suffisante pour les besoins de l'industrie, on s'attend à ce qu'à l'avenir, la grande partie des demandes de financement soit faite pour les mêmes raisons.

La direction prévoit qu'il y aura une augmentation modeste de la valeur en dollars des demandes, l'année prochaine.

Fabrication et transformation

Le portefeuille de la fabrication et de la transformation reste très diversifié, mais la grande partie de ses revenus est produite par le commerce d'exportation. Nos clients sont des entreprises qui oeuvrent dans un large éventail de secteurs, entre autres, la production biochimique, la transformation des produits de grignotage, la fabrication de produits métalliques pour l'industrie et le détail, la construction de bateaux, la transformation des aliments, la fabrication des composantes de moyens de transport en commun et la transformation à valeur ajoutée de ressources primaires, pour n'en mentionner que quelques-uns. Dans l'ensemble, ce portefeuille est demeuré presque inchangé (diminution de 0,4 %), bien qu'il ait reçu 18 demandes. Nous continuons d'accepter les demandes des nouveaux clients, mais la croissance continue d'être générée principalement par notre clientèle actuelle.

L'agence a reçu 18 demandes cette année, qui s'élevaient à 13 007 600 $, alors qu'elle en a reçu 19 demandes l'année précédente. Quinze des demandes reçues ont été acceptées et trois ont été rejetées. Hors deux demandes importantes, la demande moyenne se chiffrait à 156 725 $. En fin d'année, les engagements en matière de prêts consentis à l'industrie de la fabrication et de la transformation s'élevaient à 55 409 557 $, soit 35,6 % du portefeuille total de l'agence.

Bien que l'agence soit un prêteur stratégique, elle fait preuve, à l'instar des financiers traditionnels, de tout le soin voulu lors de l'évaluation des risques associés à toute demande. Dans certains cas, les risques sont supérieurs, toutefois, les aspects stratégiques des demandes justifient un investissement dont l'emprunteur ne pourrait pas disposé autrement afin de générer une nouvelle activité économique particulière à l'Île. Pendant la période considérée, un prêt particulièrement élevé a occasionné la perte appréciable déclarée. Bien que ce soit regrettable, c'est le prix qu'il faut payer pour faire des affaires à titre de société de la Couronne et c'est pourquoi nous établissons des provisions pour pertes sur prêts. Toutefois, nous ne prévoyons pas d'autres passations par pertes et profits que celles pour lesquelles une provision pour mauvaises créances avait déjà été créée.

Du point de vue du risque, notre portefeuille de la fabrication et de la transformation demeure vigoureux dans l'ensemble. Même si l'instabilité due aux fluctuations des devises étrangères a eu, dans certains cas, un effet défavorable sur la rentabilité de certains de nos clients, elle n'était pas de l'ordre à compromettre nos investissements.

Nous continuons de nous concentrer sur le maintien d'un équilibre entre la fourniture de prêts solides à des entreprises déjà établies à l'Île et le soutien de nouvelles entreprises, lorsque les risques sont jugés acceptables.

Pêche et aquaculture

Pendant l'année financière 2003-2004, 22 demandes ont été reçues, ce qui faisait 2 millions de dollars en tout de financement demandé. Vingt-et-une de ces demandes ont été approuvées pour un total de 1,9 million. L'autre demande a été retirée. Cela représente trois demandes de plus et une augmentation de 300 000 $ de financement requis par rapport à l'année précédente.

Sept des demandes approuvées ont été accordés en prêts de fonds de roulement à six entreprises d'élevage des moules et à une entreprise de pêche du homard. Les 14 autres demandes approuvées l'ont été pour du financement à terme pour l'achat de bateaux, d'équipement, d'entreprises de pêche et/ou pour la consolidation de dette. Onze de ces prêts ont été consentis à des clients de la pêche traditionnelle et quatre, à des éleveurs de moules.

Le portefeuille de la clientèle de la pêche et de l'aquaculture a diminué, ayant passé de 108 à 104 clients par rapport à l'année précédente. Toutefois,

notre investissement total dans ce secteur est passé de 10,7 à 11,7 millions de dollars. Par suite des difficultés survenues dans l'ostréiculture, sept autres clients, représentant des prêts regroupés s'élevant à 2,5 millions de dollars, ont été classés comme emprunteur défaillant. Ces clients sont à différentes étapes de dissolution de leur entreprise et/ou sont en procédure de faillite. On s'attend à ce qu'en fin de compte, les pertes de l'agence s'élèvent au-delà de 2 millions de dollars. On s'attend à ce que quatre seulement des cinq entreprises ostréicoles clientes de l'agence dont les prêts sont en cours pourront maintenir leur viabilité à long terme et honorer leurs engagements.

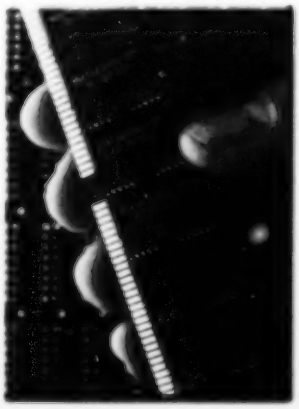
Dans le secteur de la pêche du homard traditionnelle, il y a eu une augmentation des prises débarquées sur la côte Nord et les clients ont respecté les modalités de remboursement de l'agence. Les pêches du homard du printemps et de l'automne dans le détroit de Northumberland ont connu en revanche une diminution des prises débarquées, entrainant la renégociation par l'agence des modalités de remboursement au cas par cas. Plus spécifiquement, à cause de la diminution de la pêche dans le détroit de Northumberland, huit prêts de clients ont été remaniés afin de capitaliser les arrérages et tâcher de réduire le montant des remboursements afin de tenir compte des niveaux de revenus. Si les prises débarquées de homard continuent à baisser dans le détroit de Northumberland, des effets dramatiques se feront sentir sur le portefeuille des pêches de l'agence étant donné que 40 de nos clients (sur un total de 92) pêchent dans cette zone.

Il est à espérer qu'à l'avenir l'augmentation de la taille de la carapace du homard permettra le retour à des prises débarquées de homard plus importantes dans le détroit de Northumberland, assurant ainsi le remboursement futur des comptes de crédit de l'agence. Entre temps, l'agence devra continuer de remanier les contrats de prêts existants, au besoin, lorsque la capacité d'effectuer ses paiements au fil du temps a été démontré. Autrement, de nombreux pêcheurs seront forcés d'abandonner l'industrie, ce qui entrainerait inévitablement une perte pour l'agence.

À l'heure actuelle, l'agence continue d'administrer le portefeuille et de le suivre de près afin de réduire le risque de pertes possibles.

Technologie de l'information

Le défi que doivent généralement relever les établissements de financement reposant sur l'actif, c'est de trouver des moyens d'étendre le financement aux entreprises qui oeuvrent dans cette industrie, compte tenu de la structure même du bilan de ces entreprises qui est composé essentiellement d'actifs incorporels, tels que des logiciels, des frais de développement reportés, des droits d'auteur, des brevets et ainsi de suite. En plus de l'instabilité associée avec cette industrie, le financement est souvent assuré par un utilisateur final, du capital de risque, un investisseur providentiel ou des fonds propres du propriétaire, à la place de l'engagement d'une dette.



À la suite de la modification du *Lending Agency Regulations* (règlement de l'Agence de crédit) qui établissait la technologie de l'information comme un secteur distinct, le défi qu'a dû relever l'agence fut de trouver une solution acceptable pour tous les partenaires financiers laquelle devait prévoir une combinaison de capitaux d'emprunts et de capitaux propres pour assurer la réalisation des projets de TI. La tâche n'est pas toujours facile.

Depuis mars 2001, alors que les engagements de l'agence dans les entreprises de TI s'élevaient à 3,3 millions de dollars, il y a eu une diminution continue du portefeuille jusqu'à son niveau actuel de 1,5 million de dollars, ce qui en fait le plus petit portefeuille de secteur de l'agence, lequel ne représentant que 1 % du total de l'encours de prêts.

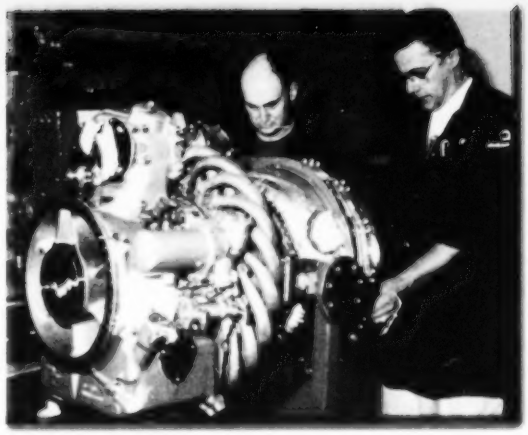
Aérospatiale

Les compagnies qui se classent dans ce secteur s'occupent soit de la construction ou de la fourniture de pièces d'aéronef. Actuellement, l'agence accorde du financement à des entreprises de réparation et de révision d'aéronefs à voilure fixe, de fabrication d'équipement d'origine et d'entretien des avions commerciales de passager. L'agence n'a reçu aucune demande de prêt pour la période ayant pris fin le 31 mars 2004 et elle n'a enregistré aucune croissance du portefeuille, ce qui peut être attribué à un certain nombre de raisons.

Premièrement, Slemon Park a connu une expansion énorme de ses installations au cours des 3 ou 4 dernières années, avec l'établissement de MDS-PRAD Technologies Corporation et les agrandissements de Testori Americas International et de Atlantic Turbines Inc. Nous nous attendons maintenant à ce que sa croissance soit maintenant minime et que les efforts déployés antérieurement s'exprimeront plutôt par des ventes.

Deuxièmement, les grandes multinationales ont, pour la plupart, une capacité d'autofinancement. Les sociétés basées à Slemon Park, qui sont des compagnies dont les actions sont cotées en bourse ou dont la capacité d'emprunt leur permet d'accéder directement à des fonds à partir des marchés monétaires, sont capables de financer leur expansion et leurs besoins en fonds de roulement à un prix beaucoup moins élevé que celui que pourrait leur faire un établissement de financement traditionnel ou l'agence.

Dans l'ensemble, le risque d'entreprise connexe n'est pas bien réparti entre un grand nombre de clients, mais malgré l'instabilité et l'incertitude des activités au sein de cette industrie, les clients de l'agence continuent d'avoir de bons résultats. Les crédits consentis à la fin de l'exercice s'élevaient à 19 980 000 $, soit 12,8 % de l'ensemble du portefeuille de prêts.



Corporate Directory

As of March 31, 2004

Appendix A

Executive

William R. Noonan
Chairman

Brian MacPhee
Vice-Chairman

Peter A. Wilson *
Secretary-Treasurer and Chief Executive Officer

Members of the Board

George Beck
Montague, PE

Wendy Ripley
Charlottetown, PE

Earl Davidson
Kensington, PE

Gerard LeClair
Central Kildare, PE

Michael L. O'Brien, FCA
Deputy Provincial Treasurer

Paul R. Jelley
Deputy Minister
Department of Development and Technology

* Non-voting

Organizational Chart

Appendix B

Auditor's Report

Appendix C

ARSENAULTBESTCAMERONELLIS
CHARTERED ACCOUNTANTS

ArsenaultBestCameronEllis
Prince Edward Place
80 Water Street
PO Box 455
Charlottetown, Prince Edward Island
Canada C1A 7L1
Telephone (902) 368-3100
Fax (902) 566-5074

April 30, 2004

Auditors' Report

To the Board of Directors

We have audited the balance sheet of **P.E.I. Lending Agency** as at March 31, 2004 and the statements of earnings and cash flows for the year then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at March 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

ArsenaultBestCameronEllis

Chartered Accountants

Financial Statements

Appendix D

P.E.I. Lending Agency

Balance Sheet

As at March 31, 2004

	2004 $	2003 $
Assets		
Cash	163,008	25,936
Accounts receivable (note 10)	253,298	873,354
Due from Province of Prince Edward Island (note 3)	8,831,778	12,139,870
Loans receivable (note 4)	141,083,593	142,024,400
Leased property (note 5)	771,795	1,010,711
Property holdings (note 6)	656,480	2,116,250
Investment in private company preferred shares	521,972	495,000
	152,281,924	158,685,521
Liabilities		
Accounts payable and accrued liabilities (note 10)	747,448	719,038
Due to Province of Prince Edward Island (note 3)	227,744	3,950,444
Notes payable (note 7)	151,306,692	155,392,536
	152,281,884	160,062,018
Contingent liabilities (note 8)		
Shareholders' Equity		
Retained earnings (deficit) - Beginning of year	(1,376,497)	828,124
Excess revenue (expense) for the year	1,376,537	(2,204,621)
Retained earnings (deficit) - End of year	40	(1,376,497)
	152,281,924	158,685,521

Approved by the Board of Directors

Director

Director

P.E.I. Lending Agency

Statement of Earnings

For the year ended March 31, 2004

	2004		2003
	Budgeted (Unaudited)	**Actual**	**Actual**
	$	**$**	**$**
Revenue			
Grants from Province	806,400	4,529,100	790,680
Interest from borrowers	10,741,668	10,460,870	10,567,515
Interest from deposits	30,000	29,039	36,836
Agricultural leases	69,996	75,493	132,115
Service fees	60,000	104,615	97,513
Post-receivership income	-	-	14,589
	11,708,064	15,199,117	11,639,248
Expenses			
Office supplies and printing	23,100	20,610	20,904
Telecommunications	14,796	11,540	10,868
Rent and occupancy	107,796	105,716	100,992
Meetings and hosted conferences	3,996	3,897	4,922
Computer equipment	9,996	10,585	13,198
Advertising and promotion	3,000	5,499	8,175
Office equipment rentals	9,504	5,487	4,204
Library and subscriptions	1,200	1,750	2,413
Repairs and maintenance	6,000	273	-
Miscellaneous	1,500	(8,881)	32,495
Professional services	42,000	82,542	25,340
Salaries and benefits	985,044	802,201	884,447
Travel and training	46,692	23,276	21,980
Interest (note 10)	8,875,692	8,752,937	8,763,487
Provision for possible losses	1,577,748	4,005,148	3,950,444
	11,708,064	13,822,580	13,843,869
Excess revenue (expense) for the year	-	1,376,537	(2,204,621)

P.E.I. Lending Agency

Statement of Cash Flows

For the year ended March 31, 2004

	2004 $	2003 $
Cash provided by (used in)		
Operating activities		
Excess revenue (expense) for the year	1,376,537	(2,204,621)
Item not affecting cash		
Increase (decrease) in due from Province of Prince Edward Island - allowance for possible losses	3,308,092	(3,950,444)
	4,684,629	(6,155,065)
Net change in non-cash working capital items		
Decrease in accounts receivable	620,056	470,083
Increase (decrease) in accounts payable and accrued liabilities	28,410	(2,091,946)
Increase (decrease) in due to Province of Prince Edward Island - current operations	(3,722,700)	1,700,746
	1,610,395	(6,076,182)
Financing activities		
Decrease in leased property (net)	238,916	1,214,530
Decrease (increase) in loans receivable (net)	940,807	(6,626,952)
Increase in notes payable	13,300,000	23,550,000
Retirement of notes payable	(17,385,844)	(10,231,592)
Increase in investment	(26,972)	(495,000)
	(2,933,093)	7,410,986
Investing activities		
Additions to and purchases of property holdings	(849,101)	(4,829,636)
Reductions and proceeds on disposal of property holdings	2,308,871	2,953,202
	1,459,770	(1,876,434)
Change in cash	137,072	(541,630)
Cash - Beginning of year	25,936	567,566
Cash - End of year	163,008	25,936

1 Status of the corporation

P.E.I. Lending Agency is a Crown corporation established by a proclamation of the Lending Agency Act dated December 31, 1998. The Agency's financial results are included in the public accounts of the Province of Prince Edward Island.

2 Summary of significant accounting policies

These financial statements have been prepared in accordance with generally accepted accounting principles.

a) Due from (to) the Province of Prince Edward Island

i. Current operations

The budgeted provision for possible losses expense is established as part of the normal budget process and is updated to reflect known changes as they become evident during the year. The actual provision for possible losses recorded in the company's accounts is expensed with a corresponding increase recorded in the allowance for possible losses in the balance sheet.

Prior to the March 31, 2004 year end, an amount equal to the annual provision for possible losses (expense or recovery) was recorded as an increase in "Due to Province of Prince Edward Island - Current Operations" and a corresponding increase in "Due from Province of Prince Edward Island - Allowance for Possible Losses".

ii. Allowable for possible losses

Prior to the March 31, 2004 year end, an amount equal to the annual provision for possible losses (expense or recovery) was recorded as an amount "Due from the Province of Prince Edward Island - Allowance for Possible Losses" and a corresponding increase in the amount "Due to Province of Prince Edward Island - Current Operations". Currently, the "Due from Province of Prince Edward Island - Allowance for Possible Losses" is reduced when a write-off of a foreclosed project is recognized by both P.E.I. Lending Agency and the Province, with notes payable reduced correspondingly.

Subsequent to March 31, 2003, the P.E.I. Lending Agency will not be required to refund to the Province the current year's provision for possible losses and as such will be required to fund increases in the allowance for possible losses after March 31, 2003. The $8,831,778 balance in "Due from Province of Prince Edward Island - Allowance for Possible Losses" at March 31, 2004 will be funded by the Province.

b) Loans receivable

Working capital loans are issued to qualified lenders and are recorded at cost less an allowance for possible losses. These loans bear interest at the Toronto Dominion Bank prime rate plus 1 ¾% to 2 ¾% and are repayable at the end of each sector's operating season or specific project.

Mortgage loans consist of loans issued to Prince Edward Island enterprises for purposes of acquiring capital assets. These loans are recorded at cost less an allowance for possible losses. These loans are issued at long-term interest rates and are repayable over various terms to a maximum of 20 years with interest rates ranging from 5.19% to 12.25%.

Interest income is recorded on the accrual basis until such time as the loan is classified as non-current. A loan is classified as non-current when the Corporation has been unsuccessful in its attempt to collect arrears payments or have the loan satisfied.

An impaired loan is a loan in arrears in excess of 120 days or where in management's opinion there is no longer reasonable assurance as to the timely collection of the full amount of the principal and interest.

c) Allowance for possible losses

An allowance is maintained which is considered adequate to absorb all credit losses and off-balance sheet items including guarantees. The allowance is deducted from the applicable asset on the balance sheet, except for guarantees. The allowance for guarantees of $50,000 (2003 - $50,000) is included in accounts payable.

The allowance consists of specific and general provisions.

Specific provisions include the accumulated allowances for losses on particular assets required to reduce the book values to estimated realizable amounts. Specific provisions total $10,661,633 (2003 - $9,683,461).

The company reviews its loan portfolios and leased properties on an ongoing basis to assess whether a loan should be classified as impaired, or an allowance or write-off recorded.

A variety of methods are used to determine the amount expected to be recovered from impaired loans and property holdings, including estimated future cash flows and the estimated fair value of the underlying security and value of any collateral security taken.

A general provision of $2,138,457 (2003 - $2,406,411) includes accumulated allowances for losses which are prudential in nature and cannot be specifically identified. The general provision is based on past performance of similar loans, the level of the specific provision, management's judgement, the economic climate and the maturity and financial strength of the investee.

d) Leased property

Leased property represents the cost to acquire agricultural property based on appraised market value at the inception of the lease less an allowance for possible losses. Operating leases are negotiated with the lessee for a maximum of 5 years at a rate of interest tied to commercial lending rates. The lease rates currently range from 7.5% to 10.5%. The lease may be renewed for one five-year term after which time the lessee must repurchase the property

Lease income is recorded on an accrual basis until the lease is repaid or the property is transferred to property holdings foreclosed projects. When a lease is in arrears in excess of 120 days or when in management's opinion there is no longer reasonable assurance of the timely collection of the full amount of principal and interest, the lease is classified as impaired.

e) Property holdings and amortization

Office furniture and equipment and computer equipment are fully expensed in the year of acquisition. The amount expensed during the year ended March 31, 2004 was $11,267 (2003 $13,198).

Foreclosed projects are carried at the lower of cost of the impaired asset prior to realization of the related security and the underlying estimated realizable value of the security

The reduction from cost to estimated realizable value is recorded as an allowance for possible losses.

f) Investment in private company

Investment in preferred shares of a private company is recorded at the lower of cost or estimated realizable value.

It is not practical within constraints of timelines and cost to determine the fair value of the investment as it is a closely held private company that has no organized financial market. The estimated realizable value of this investment is based on expected future cash flows.

g) Pension liabilities

The Corporation's staff are members of the Province of Prince Edward Island pension plan. The pension plan obligation is a liability of the Province and not the Corporation and no liability for these costs has been accrued by the Corporation at March 31, 2004.

h) Estimated realizable value of financial instruments

Estimated realizable value (fair value) is subjective in nature requiring a variety of valuation techniques and assumptions. The company's financial instruments are not exchangeable and it is difficult, and often not practical, to determine their estimated realizable value. Where it is possible to estimate realizable value, the company assumes that it will not sell the assets or the liabilities, taking into account only changes in credit risk as credit risk is the main cause of change in the estimated realizable value of the company's financial instruments. Credit risk is defined as the risk that the note holder will fail to discharge an obligation in whole or in part resulting in a financial loss to this company

i) Management estimates

The presentation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reported period. Actual results could differ from those reported.

3 Due from (to) the Province of Prince Edward Island

	2004 $	2003 $
Current operations		
Balance - Beginning of year	(3,950,444)	(2,249,698)
Current year's actual provision for possible losses	-	(3,950,444)
Repaid to the province	-	2,249,698
Grant receivable	3,722,700	-
Balance - End of year	(227,744)	(3,950,444)
Allowance for possible losses		
Balance - Beginning of year	12,139,870	8,189,426
Current year's expense	-	3,950,444
	12,139,870	12,139,870
Less: write-offs during the year	3,308,092	-
Balance - End of year	8,831,778	12,139,870

4 Loans receivable

					2004	2003
		Impaired loans	Allowance for possible losses			
	Total	included in total	General	Specific	Net	Net
	$	$	$	$	$	$
Working capital loans	26,104,215	4,798,498	388,457	1,108,206	24,607,552	22,897,047
Mortgage loans receivable						
Agriculture	7,791,814	1,248,723	100,000	150,000	7,541,814	8,664,020
New farmer	32,915	32,915	-	-	32,915	32,379
Tourism	15,536,820	1,277,652	250,000	-	15,286,820	14,807,038
Manufacturing and processing	43,253,481	167,641	200,000	42,739	43,010,742	44,268,416
Fisheries	7,454,325	1,213,437	-	165,000	7,289,325	6,482,526
Aquaculture	145,629	127,384	-	85,000	60,629	814,585
Small business	10,835,313	117,605	-	65,200	10,770,113	11,790,209
Blueberry	9,689,306	2,549,128	1,200,000	840,000	7,649,306	7,190,305
Cranberry	1,739,571	489,423	-	300,000	1,439,571	1,292,635
2000 Hog Program	68,970	-	-	-	68,970	69,760
Aerospace	18,851,043	-	-	-	18,851,043	19,945,737
Information technology	1,503,704	-	-	-	1,503,704	2,067,608
Other	8,503,710	7,425,988	-	5,532,621	2,971,089	1,702,135
	125,406,601	14,649,896	1,750,000	7,180,560	116,476,041	119,127,353
	151,510,816	19,448,394	2,138,457	8,288,766	141,083,593	142,024,400

5 Leased property

					2004	2003
		Impaired loans	Allowance for possible losses			
	Total	included in total	General	Specific	Net	Net
	$	$	$	$	$	$
Agricultural leases	867,795	182,625	-	96,000	771,795	1,010,711

6 Property holdings

	2004 $	2003 $
Foreclosed projects - land, buildings and equipment held for resale	2,933,347	5,799,655
Less: Allowance for possible losses	2,276,867	3,683,405
	656,480	2,116,250

7 Notes payable

	2004 $	2003 $
Short-term promissory notes	16,551,802	17,550,000
Long-term	134,754,890	137,842,536
	151,306,692	155,392,536

Short-term promissory notes are issued to the Province of Prince Edward Island with interest set monthly based on the Province's short-term lending rate in existence at the first day of the month. These notes are renewed on an ongoing basis with interest payable monthly.

The notes payable - long-term are issued to the Province of Prince Edward Island and have various repayment terms and interest rates ranging from 4.95% to 8.50%.

The aggregate amount of principal payments required in each of the next five years to meet retirement provisions is as indicated below. Certain notes becoming due during the next five years have been assumed to be refinanced under similar terms:

	$
For the year ending March 31, 2005	8,535,649
2006	7,012,477
2007	5,904,976
2008	6,178,034
2009	5,136,626

8 Contingent liabilities

As of March 31, 2004, P.E.I. Lending Agency was contingently liable under a loan guarantee on behalf of a development company in the amount of $81,563 (2003 - $110,867) for which P.E.I. Lending Agency has included $50,000 in its allowance for possible losses. This portion of the allowance for possible losses is included in accounts payable. The guarantee is secured by a realty mortgage, and proceeds from liquidation are expected to cover the remaining amount of the guarantee.

9 Commitments

The P.E.I. Lending Agency loans approved but not disbursed at March 31, 2004 amount to $9,270,003 (2003 $745,300).

10 Related party transactions

Balance Sheet

Included in accounts receivable is $250,586 (2003 $866,747) due from the Province of Prince Edward Island.

Included in accounts payable and accrued liabilities is $567,817 (2003 $521,949) in accrued interest payable to the Province of Prince Edward Island.

Statement of earnings

Included in expenses is $8,752,937 (2003 $8,763,487) in interest paid/payable to the Province of Prince Edward Island.

The above transactions were recorded in the normal course of operations and measured on the same terms as transactions with unrelated parties.

11 Operating lease

The minimum annual lease payments required in each of the next two years under an operating lease expiring March 31, 2005 is $40,588 in base rent plus common area expenses of approximately $60,000 annually

12 Interest rate risk

The following table sets out the assets and liabilities on the earlier of contractual maturity or repricing date. Use of the table to derive information about the Agency's interest rate risk position is limited by the fact that borrowers may choose to terminate their financial instruments at a date earlier than contractual maturity or repricing date. Examples of this include mortgages, which are shown at contractual maturity but which could prepay earlier.

	Within 1 year $	After 1 year but within 5 years $	After 5 years $	Not interest rate sensitive $	Provision for possible losses $	Total $
Assets						
Cash	163,008					163,008
Accounts receivable				253,298		253,298
Due from Province of Prince Edward Island				8,831,778		8,831,778
Loans receivable	39,090,769	64,252,076	48,167,971		(10,427,223)	141,083,593
Leased property	867,795				(96,000)	771,795
Property holdings				2,933,347	(2,276,867)	656,480
Investment			521,972			521,972
Total assets	40,121,572	64,252,076	48,689,943	12,018,423	(12,800,090)	152,281,924
Liabilities and surplus						
Accounts payable and accrued liabilities				697 448	50,000	747 448
Due to Province of Prince Edward Island				227 444		227 444
Notes payable	25,087 451	24,232,113	101,987,128			151,306,692
Surplus				340		340
Total liabilities and surplus	25,087 451	24,232,113	101,987,128	925,232	50,000	152,281,924
Interest rate sensitivity gap	15,034,121	40,019,963	(53,297,185)	11,093,191	(12,850,090)	
Cumulative interest rate sensitivity gap	15,034,121	55,054,084	1,756,899	12,850,090		

Clarification to Note 4 of Financial Statement

Appendix E

Column 1 – Total
Represents the total loan/leases divided by economic sector. These balances represent the balance owing at March 31, 2004, before any provision for loss. The "other" category is comprised of loans classified as non-current, wherein interest is no longer being accrued.

Column 2 – Impaired
Represents loans in arrears in excess of 120 days, or where in management's opinion, there is no longer reasonable assurance as to the timely collection of the full amount of the principal and interest. Management's assessment is based on the extent of the arrears, the value of collateral security, the cash flow of the borrower and management's judgement. The impaired loans are included in the total loan/leases in Column 1.

Column 3 – General Provision
A provision for loss based on management's judgement by sector whereby adverse economic trends suggest losses may occur, but where such losses cannot yet be determined on an item-by-item basis. Management takes into consideration past performance of similar loans, the level of specific provision and the existing economic climate.

Column 4 – Specific Provision
Indicates the provision required to reduce particular assets from their book value to their estimated realizable value. Management takes into account the estimated future cash flow of the borrower and the estimated fair value of the collateral security held of the borrower.

Column 5 – Net
Indicates the total loan/lease (column 1), less the general and specific provisions for loss (columns 3 and 4).

Application Statistics
April 1, 2003 to March 31, 2004

Appendix F

Sector	Total Received		Amount Approved		Declined/Withdrawn	
	No.	Amount	No.	Amount	No.	Amount
Agriculture	32	5,948,000	31	5,859,000	2	89,000
Fisheries	21	1,994,355	21	1,994,355	0	0
Manufacturing and Processing	18	13,007,600	15	12,307,600	4	700,000
Aerospace	0	0	0	0	0	0
Information Technology	2	2,530,000	1	30,000	1	2,500,000
Small Business	20	3,305,830	16	2,878,830	4	427,000
Tourism	18	9,208,500	16	3,336,500	3	72,000
Fur Program	9	714,395	9	714,395	0	0
Beef Program	52	162,960	52	162,960	0	0
Total	**172**	**36,871,640**	**161**	**714,395**	**14**	**3,788,000**

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